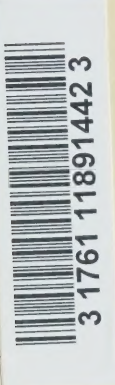


BEFORE THE RESTRICTIVE TRADE PRACTICES COMMISSION

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IN THE MATTER OF A GENERAL INQUIRY  
UNDER SECTION 47 OF THE COMBINES  
INVESTIGATION ACT RELATING TO THE  
MANUFACTURE, PRODUCTION, DISTRIBUTION,  
PURCHASE, SUPPLY AND SALE OF TELE-  
COMMUNICATION SYSTEM AND EQUIPMENT




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FINAL ARGUMENT OF THE MINISTER OF TRANSPORTATION AND  
COMMUNICATIONS ON BEHALF OF THE GOVERNMENT OF ONTARIO

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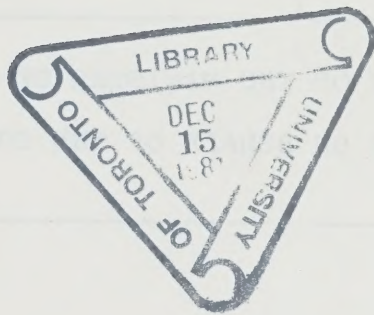
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## INTRODUCTION

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### PART I

## INTRODUCTION

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## INTRODUCTION

The Restrictive Trade Practices Commission Inquiry has raised issues of great significance to the economy of Canada. Telecommunications, both in the manufacturing and carrier sectors of the industry, is part of the essential infrastructure of a modern state, particularly one as large and as sparsely populated as Canada. The importance of this industry as an employer and contributor to the Canadian economy is being overshadowed by the increasing importance of its role as an "electronic highway" permitting the rapid growth of other information intensive industries. An efficient and innovative telecommunications industry is crucial to the economic growth of every industrial state. For Canada, moreover, this importance is increased since the telecommunications equipment industry is a rare example of a domestically-based manufacturing industry which is both technologically advanced and internationally competitive.

The Government of Ontario has considered very carefully the evidence presented by the Director of Investigation and Research, Combines Investigation Act, both in "The Effects of Vertical Integration on the Telecommunication Equipment Market in Canada" (The Green Book), as well as the evidence adduced by all other parties, including the evidence presented by Bell Canada and Northern Telecom. Ontario's interest in these hearings arises because of the enormous implications of the issues for the economic well-being of the Province.

The initial statement of the Government of Ontario quoted the then Treasurer of the Government of Ontario regarding the Government's intention to encourage the growth of efficient, internationally competitive industries. This





goal remains Government policy. Premier William Davis stated in "Building Ontario in the 1980's" that it was a basic objective, and that

"To ensure international competitiveness and achieve economic growth, the Government will promote research and development, nurture high technology, and expand markets for Ontario products".

The telecommunications industry is a prime example of such an industry. Allegations that the integrated relationship between Bell Canada and Northern Telecom was impairing the healthy growth of both the manufacturers and of the efficient operations of Bell Canada have therefore been considered most carefully.



PART II

STATEMENT OF THE ISSUES



The Government of Ontario has considered all the matters raised during the course of the hearing. It is our view that there are two fundamental issues at stake. These are:

1. The costs and benefits of vertical integration for the telecommunications equipment manufacturing industry in terms of its employment, economic efficiency, balance of trade, technological sovereignty, and its international competitiveness, and
2. The costs and benefits of vertical integration for the Bell Canada subscriber both in terms of its impact on Bell Canada's innovativeness and efficiency and on the range of services offered by Bell Canada.

Ontario has participated in these proceedings in order to assess evidence for and against vertical integration. The record has been carefully reviewed to find evidence pertaining to the above-noted issues and to determine where the public interest lies.



PART III

THE BURDEN OF PROOF





In conducting this Inquiry, the Restrictive Trade Practices Commission is examining long standing historical relationships between operating telephone companies and their manufacturing subsidiaries. In doing so, it must consider whether the status quo or some other arrangement is in the public interest. It is our view that the proponents of change have a very heavy burden to discharge in satisfying the Commission and the public that change is for the public good.

Before assessing the evidence presented to the Commission, we consider it necessary to demonstrate that in this case the burden of proof should be placed on those who seek change. In deciding where the burden should fall, Ontario has considered the following factors:

- A. The present performance of the equipment manufacturing and carrier industries: specifically, whether these industries are on the whole serving the public good, and
- B. The risks associated with the changes proposed by the Director: this involves a consideration of the degree of uncertainty as to the effects of the proposed major structural changes and of the consequences of being in error.



A. The Present Performance of the Industries  
The Manufacturing Industry

The telecommunications equipment manufacturing industry employed over 40,000 Canadians in 1978.<sup>(1)</sup> It has since grown both in size and in technical sophistication. The industry is dominated by Northern Telecom, which employed over 18,000 Canadians in 1978. The only other Canadian company manufacturing a broad range of telecommunications equipment is AEL Microtel, a subsidiary of British Columbia Telephone Company, which employed 3,000 Canadians in the same year. Next, there is a group of fourteen middle sized firms which employed about 13,000 Canadians in 1978. Finally, there is a large group of highly specialized manufacturers with annual sales of less than \$10 million.

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1. Department of Communications, "The Supply of Communications Equipment in Canada", RTPC, T-1935, Ch. 1.



In assessing the performance of the industry's manufacturing sector, one is struck by the rapid growth of its small, specialized members, who have succeeded in establishing themselves in a variety of market niches. Though an atypical example, Mitel's sales volume increased from \$1,526,000 to approximately \$40,000,000 between 1976 and 1980 (RTPC, T-1935, p.70). Moreover, from 1975 to 1979, Mitel's sales to Bell averaged 12.26 % of its total sales (RTPC, vol. 169, pp. 25284-22585). Gandalf's sales grew at an average annual rate of more than 50% to \$13,000,000 in the fiscal year ending July, 1979 (RTPC, T-1935, p.66). In 1980, Gandalf's sales were estimated at \$21,000,000 (RTPC, T-1935, p.66). A larger firm, AEL Microtel, showed a sales growth of 25%, going from \$150,000,000 in 1978 (RTPC, T-1 35, p.33) to \$188,000,000 in 1980.

However, it is Northern Telecom's performance which will largely determine the economic performance of this industry as a whole, since it is the only Canadian company large enough to compete internationally across a broad range of telecommunications equipment.

Mr. Grandy, former Deputy Minister of Consumer and Corporate Affairs, described Northern Telecom's role in the development and export of telecommunication equipment as follows:



Northern Telecom is, today, the only Canadian-owned high technology manufacturer that is large by international standards (it appears to rank sixth or seventh in the world in sales of telecom type equipment). It manufactures a broad line of equipment which it markets to telephone companies throughout Canada thereby giving a high degree of technological independence to Canada in this vitally important industry. It undertakes major R & D programs and spends more on R & D than any other manufacturer in Canada. I understand that it does not rely on government funding. Its products are in the forefront of technology and are acclaimed internationally. Its exports from Canada are substantial. (RTPC, T-1884, p.41).

A critical indicator of this economic performance is the Company's ability to compete successfully in international markets. Mr. Davies, Vice-President of Business Development, Northern Telecom Ltd., indicated at p.31868 of the transcript and in T-1819 that the value of export sales as a percentage of the value of Northern Telecom Canada Ltd.'s total sales is becoming relatively more important.

Specifically, NTCL's export sales in 1979 were 16.5% of NTCL's total sales. Translating these figures into employment terms, the manufacture, sale, and distribution of these goods for export accounted for 3,000 jobs in Canada in the same year. Mr. Davies predicted that NTCL's export sales in 1980 would increase to 25 percent of its Canadian manufacturing. Furthermore, Mr. Millar, Executive Vice-President, Operations, Northern Telecom Ltd. testified at pp.32493-32495 of the record that Northern Telecom has on average a depth of manufacturing of 68 percent in 1978, implying that most of the value of these export sales is domestically produced.





These figures become even more significant when compared to other sectors of the Canadian electronics industry. Tables 42, 43 and 46 of Exhibit T-1566-C, which list production, imports and exports as a percentage of consumption for each of the consumer electronics, computer, and telecommunications sectors of the electronics industry, show that the telecommunications industry is the only sector which is approximately in balance. In the remaining sectors, there is a deficit in the balance of trade.

Not only, then, has Northern Telecom been able to grow and to compete internationally, but other firms in the industry have experienced significant growth in recent years. Indeed, some of the smaller firms in Canada have only developed in recent years, indicating that there was room for them in the industry.

#### The Carrier Industry

Canada has benefitted from a high quality telecommunications system. Ontario believes that Bell Canada's overall performance has been and continues to be excellent, providing high quality telephone services at reasonable rates. Bell Canada is known and respected throughout the world for the quality of the service it provides; it has placed Canada in the forefront of the telecommunications technology. The Consultative Committee on the Implications of Telecommunications for Canadian Sovereignty stated that "the Canadian telephone system, despite its fragmented composition, operates with a high standard of efficiency and quality" (RTPC, T-1160, p.23).



Ontario believes that the recognition by the international community of this excellence, as evidenced by the major contract signed by Saudi Arabia for Bell Canada's assistance in the development of a modern telecommunications system, suggests that the existing relationship has served the national interest well.

#### Conclusions Regarding the Present Performance of the Industries

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Ontario concludes that no obvious problems exist in either the manufacturing or carrier industries and that these industries are, on the whole, serving the public interest. Northern Telecom has grown; it has been able to compete internationally, and it supports Canada's largest private R & D program. There are a growing number of flourishing small and medium sized firms whose growth should accelerate as the terminal equipment market becomes increasingly accessible. This evidence conveys a picture of a flourishing industry rather than one stifled by the absence of competition. Similarly, Bell Canada has created one of the most advanced telecommunications systems in the world, offering a wide variety of new services. The telecommunications industry in Canada then certainly does not constitute an industry which is facing major problems.

#### B. Risks Inherent in Divestiture

The Director recommended that the best solution to the issues raised in his report is:

...the introduction of increased competition in the telecommunication equipment industry. Furthermore, the most effective long-term method to achieve this goal is through the divestiture of Northern Electric from Bell Canada as a means of reducing existing barriers to entry into the telecommunication equipment industry. (Green Book, p.184).



Various witnesses have testified that divestiture would terminate Northern Telecom's status as a preferred supplier to Bell Canada. In fact, this was considered by the Director to be one of the benefits of divestiture, since it would allegedly spur innovation.

The divestiture will benefit the non-integrated supplier. It will give such firms an opportunity to have products evaluated on the open market. It will promote within Canada a broader based electronics industry which will make Canada more internationally competitive in the rapidly expanding telecommunication market. (Green Book, p.193).

Several Bell Canada and Northern Telecom witnesses have testified that there are substantial cost-reducing benefits to Bell Canada resulting from a vertically integrated structure. It is Ontario's view that the Director has not adequately addressed the issue of the impact which his proposed solution, divestiture, would have on these benefits. Our comments on these benefits will be given in a later section. In this section, it is necessary to comment on the potential consequences to Northern Telecom of divestiture, and of its loss of its share of the Bell Canada market.

Ontario is concerned about the potential undermining of Northern Telecom's ability to remain at the leading edge of technology, to remain internationally competitive, and to maintain its role as a major employer in Canada. The evidence demonstrates that a strong domestic base of sales is necessary to sustain Northern's position.

Mr. Grandy made the following statement in his written evidence to the Commission:



A most important requirement for the successful operation of such a firm as Northern Telecom is a large customer base. Without a reasonably assured volume market a large high-technology enterprise cannot sustain the full range of activities on which its survival depends. Manufacturers of computers, heavy electrical equipment and telecommunications equipment in every major industrial country rely on their home market as a base to provide a critical volume of business. In relatively few countries, notably the United States, is the home market sufficiently large to support several major broadline manufacturers. (RTPC, T-1884, pp.43-44).

Northern Telecom, therefore, is likely to lose its preferred position as supplier to Bell Canada. This would probably impair its ability to compete internationally.

Who would be the most likely beneficiaries of a change in the Bell-Northern relationship? In the words of the Director, "the divestiture will benefit the non-integrated supplier". (Green Book, p.193). Unfortunately, the Report did not specify precisely which non-integrated suppliers would benefit. That is, the Green Book failed to differentiate between foreign and domestic competition. This distinction, however, is critical in evaluating the effect of divestiture on the Canadian economy.

Mr. Grandy, at a different point in his evidence posed the following question:

Would the damage to Northern be offset by the development of a "broader based electronics industry in Canada?" This seems to me most improbable. Surely what we would see would be fragmentation of the market and a growing proportion of imports... (RTPC, T-1884, p.47).

The danger to Northern's international competitive position is underlined by the testimony of Mr. Davies, Executive Vice-President of Business Development for





Northern Telecom Ltd. that not only do Northern's international competitors enjoy preferred relationships with telephone companies, but also that Northern is smaller than many of its international competitors.

A comparison of the telecommunications sales figures for the three largest multinationals with those of Northern supports this observation. LME's 1978 sales, for instance, were \$2B (RTPC, T-1566, p.70); ITT's 1979 telecommunications sales were \$5.3B (RTPC, T-1566, p.74); and Siemen's 1979 telecommunications sales were \$3.1B (RTPC, T-1566, p.76). By contrast, Northern's sales in 1979 were \$1.9B (RTPC, T-1572, p.1).

Chapter 4 of RTPC Exhibit T-1566 describes the extent to which arrangements in Japan, Europe, and elsewhere, have involved Government "assistance" to domestic industry either in the form of full market protection, subsidized R & D, rationalization of local industry, or other forms of intervention and subsidy.

Some of these competitors have testified at this inquiry. Their evidence concerning their likely behaviour in Canada in the event of the opening of the Bell market, and the resulting impact on the Canadian economy, was contradictory.

For example, Siemens initially testified that increased access to the Canadian market was "a prerequisite for expansion in the area of local manufacturing."  
(RTPC, vol.32, p.5018)

But in subsequent cross-examination Siemens admitted that greater access to the Bell Canada market would not



necessarily result in an expansion of local, Canadian manufacturing and, in fact, conditions might influence expansion elsewhere:

A. Now, to what extent we will ever manufacture PBX systems in Canada cannot be determined at this time. We are looking at manufacturing in more global terms. When we pick up manufacturing activities in Canada we analyze the Canadian market, we look at the United States market, we look at the South American market, particularly Mexico and Venezuela. So, at this point in time no decision has been made as to when we will manufacture, what we will manufacture and what market would be required to justify such action; we have not gone into this type of analysis. You have to understand that any manufacturing or any decision relating to manufacturing is not a decision that is made by Siemens Electric in Canada: it is a decision that is being made by the parent company in close co-operation with Siemens Electric. So, the final decision is not necessarily ours.

Q. I think I appreciate that, thank you. But I suppose the decision would be affected by the tariff situation in Canada, labour costs and the usual factors that influence a manufacturing decision?

A. That is correct.

Q. And if it were more economic to manufacture in the United States and import into Canada, even with the existing tariff arrangement, then presumably that decision could be made?

A. That is correct.

. . .



Q. Coming back to this manufacturing decision which you were talking about, would it be fair to say, as well, that having regard to the size of the Canadian market your basic research and development would probably still continue to be done in the larger market areas, for example, at Cherry Hill; New Jersey, or the Federal Republic?

A. Well, should we experience an opening or an increase in the accessibility of the Canadian market we would not rule out research and development to be done in Canada in the future. In fact, there are some product areas where we do carry research and development locally. To name one product line would be time division multiplex.

Q. I wasn't suggesting that you wouldn't do any research and development, but what I was suggesting to you was the substantial portion of the research and development which you described to us the last day we were here would probably continue to be done in the United States or Germany? It seems to me it follows that if you haven't got a substantial sales base in Canada you are not going to have the money to spend on research and development?

A. That is somewhat on what you define as research and development. If you get into the area where you product specific research and development which is more or less development and not so much research, then we might do application research, for example, right in the country where it is required and this is what we are doing to date.

Now, this is the development of present product and changes in present product and applications of present products to make them fit the Canadian market.

Q. Let's take the case of a new product such as a new digital switch using micro-processors, micro-processor technology. I would suggest to you really that that type of research would not be done in one of the manufacturing areas where Siemens is, where there is a relatively



small market, but would probably in all probability be done either at Cherry Hill or in Germany?

A. That is very probable.

Q. Yes. So that if there are going to be any substantial changes, new changed products coming on the market from Siemens it is going to be as a result of research and development either done in Germany or in the United States?

A. Yes. (RTPC, Vol. 40, pp. 6007-6010)

Furthermore, Siemens gave the following explanation as to why switching equipment which it is presently selling to CN/CP (Infoswitch) continues to be manufactured in the United States:

...I think there is very little justification for the telex switches to be manufactured in Canada because the marketplace is too small. Due to that reason I think the majority of the manufacturers have imported the equipment from the U.S. Fredericks I think have done some work in electronics in Montreal, but they are running into difficulties. (RTPC, Vol. 40, p.6012).

Similarly, the following exchange took place between AEI Telecommunications Canada, the exclusive distributor for Nippon for all switching equipment, and counsel for the Director:

Q. Mr. Yates, does the Nippon Company have any plans to manufacture products in Canada?

A. Not to my knowledge.





Q. Could you indicate to the Commission why they have elected not to manufacture in Canada?

A. I would think it probably would be labour costs. That is they have started manufacturing in Dallas to manufacture PBX equipment.

Q. In the United States?

A. Yes.

. . .

Q. In any event, if a change along that line occurred it would assist your business?

A. Not very much. Most of the Japanese products are finished systems. We do some very small amount of assembly, but not much. It would, of course, help on spare parts. (RTPC, Vol. 23, pp. 3414-3415).

The Director attempted to show that an opening of the Bell market would have a positive impact on employment; however, his evidence was based either on theoretical economic arguments, or on the evidence of Northern Telecom's foreign competition who were asked for their likely reaction in the event of increased access to the Bell market which we have just discussed.

Much of the Director's evidence on this point consisted of simplistic application of the U.S. experience to the Canadian situation without taking into account the considerable differences between the two countries.

For example, Manley Irwin, Professor of Economics and Administration at the Whittemore School of Business and Economics at the University of New Hampshire, responded



as follows to a question by counsel for Bell Canada, regarding the liberalization of terminal attachment:

If the attachment policies were liberalized I have no doubt that foreign suppliers would seek an opportunity to sell, manufacture, build their R & D facilities to tap that market. I must say I find that paragraph an insult to Canadian industry. It really says Canadian industry cannot compete in today's world, Canadian industry cannot compete against other suppliers and it ought to exist in a hothouse environment. I just don't believe that of the Canadian economy. It is true in the United States, Mr. McIntosh, that when we relaxed interconnection the first suppliers were offshore suppliers from Europe and the far east, but the second wave of suppliers were indigenous American firms and that contributes to our employment and to our research and development base and to our investment and ultimately to our gross national product and our standard of living . (RTPC, Vol. 22, pp.3139-3140).

Mr. Irwin's testimony attempted to relate liberalized terminal interconnection to the opening of the carrier market for equipment.

If competition has benefited the telephone subscriber in buying equipment, cannot competition equally benefit the telephone utility in securing equipment? It is that question that finds U.S. telecommunications policy exploring the means whereby a closed equipment market can be exposed to the beneficial effect of rivalry and access. In short, competition in the interconnect market has rendered suspect the alleged virtues attending a closed vertical market. To that extent U.S. telecommunications is undergoing a fundamental re-appraisal . (RTPC, Vol. 21, p.2925).



Mr. Irwin's evidence largely consisted of such attempts to draw parallels between Canada and the United States despite the different social, political and economic circumstances in each country. In cross-examination it became quite clear that Mr. Irwin's knowledge of the Canadian telecommunications industry and, in particular, his knowledge of Bell Canada and Northern Telecom is at best only theoretical, with no knowledge of the specific Canadian concerns. (RTPC, Vol. 20, pp.3133-3137, 3140-3144).

It is Ontario's view that no direct implication can be drawn for Canada from the U.S. experience, since to do so would require unrealistic assumptions about the similarity between Canada's industrial strength and that of the U.S.

The degree of foreign penetration of the Canadian market is likely to be increased by the degree to which the major multinationals have constructed production facilities in the United States and are developing products for the U.S. market with its similar technical standards. As a result, an opening of the Bell market may expose Canadian manufacturers in the manner described by Mr. Davies:

A large portion of the Canadian market has always been 'open' to competition and the portion is growing as the CPE of non-Bell telcos grows in relation to the Bell CPE. Foreign suppliers have, to varying degrees and at different times, been active in those markets but, except for U.S. suppliers, different equipment interface specifications have been a major deterrent. That situation has changed however. The size of the markets available to those foreign suppliers in the U.S. is more than sufficient to justify their modifying their equipment to North American standards. As a consequence, Canada today represents an available incremental market for U.S. contenders.



That this opportunity has not yet been exploited by those competitors can be explained by the partial protection of the Bell market and the fact that Northern, with access to the Bell/Northern knowledge base, has been able to design and manufacture for sale in Canada and the United States, a broad line of cost effective telecommunications products at the 'leading edge' of technology. It remains to be seen, however, whether the situation in Canada will change as foreign competitors gather strength in the U.S. markets and some of the giants of U.S. industry make full use of their recent acquisition of telecommunications companies. (RTPC, T-1566, pp. 106-107, footnote omitted).

This theory is consistent with the direct testimony of AEI and Siemens discussed previously, which indicated that an opening of the Bell market would not result in increased employment in Canada. There is a further danger that foreign competitors may engage in the kind of competitive behaviour described below, with products being sold at incremental costs as indicated by the following exchange between Mr. Davies and Counsel for the Government of Ontario.

- Q. I know in talking to Mr. Kaiser earlier you got into this idea and I guess we got into it, too, where the multi-national would attempt to recover its front-end costs, the R & D costs, the fixed costs of getting into a particular product in its protected market and that the product will be priced incrementally in other markets. I am not sure I understand exactly on what you rely to make that statement. Is it simply Northern's own experience or are there other studies available to prove that concept?
- A. I don't know about studies but there certainly is a significant number of statements by people, some of which are referenced again in the references, one in particular there which





addresses the world market for central office switching equipment and is referring to the position of France, speaks of prices in an international market at half the price of those in the domestic market. I could probably find that reference if you would like it.

- Q. If it is in the material, no, but are there other statements or studies on which you relied than you have put in the record?
- A. Well, as mentioned in different market research reports and so on. Certainly in practice you face it.
- Q. You know that from your own experience in facing competition?
- A. You only have to look at some of the prices that are quoted.

(RTPC, Vol. 212, pp. 31809-31810).

Such practices would, of course, increase the risks associated with opening the Bell Canada market to foreign competitors. There is, therefore, a substantial danger that the opening of the Bell market to foreign competition would result in a decrease of employment in Canada without any corresponding benefits. This decrease, moreover, is likely to be irreversible since the severance of Northern Telecom's ties to Bell Canada may significantly reduce its ability to compete internationally, reducing its ability to continue to finance its R & D activities.

#### Conclusions Regarding the Burden of Proof

Northern Telecom, which has the benefit of a preferred-supplier relationship with Bell Canada, performs the majority of its R & D, administration, and its manufacturing of exports to countries other than to



the United States, in Canada. The Director has asserted that opening the Bell Canada market to competition would result in greater opportunities for other manufacturers to sell to Bell Canada, and increased manufacturing by others in Canada. These assertions are largely unsupported by the evidence.

Ontario, moreover, would oppose such a unilateral opening of the Canadian market to competition from countries whose markets are "closed" to Canadian products.

Further, divestiture could undermine Northern Telecom's ability to remain at the leading edge of technology, with resultant negative impact on both employment in Canada, and on Bell Canada's ability to continue to provide a high quality of service at reasonable cost.

These substantial risks, combined with the fact that the Canadian telecommunication industry is operating successfully, has convinced the Government of Ontario that the onus must be upon the Director to prove that divestiture is in the public interest.



PART IV

ALLEGATIONS OF THE DIRECTOR OF  
INVESTIGATION AND RESEARCH,  
COMBINES INVESTIGATION ACT



A careful review of the record of these proceedings indicates that the Director has forwarded his case for divestiture upon essentially the following allegations of the harm resulting from the existing industry structure.

These are summarized as follows:

1. That Bell has foreclosed its market to competition or equivalently that Bell Canada's procurement policy favours Northern and prevents it from purchasing the most appropriate equipment available on the market.
2. That Bell has attempted to foreclose other telephone companies' markets to competition.
3. That Northern Telecom's pricing policy has been distorted.
4. That vertical integration renders the regulation of Bell Canada ineffective.
5. That Northern Telecom and Bell Canada's incentive and ability to innovate have been reduced.
6. That telephone subscribers have had a reduced choice in the equipment available to them.

Ontario has considered each of these allegations, and the evidence bearing on these issues, to determine whether the Director has met the burden of proof as discussed in the previous section of this submission.





1. Market Foreclosure

The allegation concerning market foreclosure and the harmful effects associated with it was stated very succinctly by the Director:

The telephone operating company purchased almost exclusively from its subsidiary supplier, a practice which has resulted in a highly concentrated telecommunication equipment manufacturing industry in Canada. Furthermore, the complex engaged in a series of exclusionary tactics which reinforced the market foreclosure aspects of the non arms-length purchasing practices .  
(Green Book, p.182).

The allegation that Northern Telecom is Bell Canada's preferred supplier was largely conceded by Bell early in the inquiry; a clear statement of this policy is contained in the evidence of Mr. J.V.R. Cyr, Executive Vice-President, Administration, Quebec Region of Bell Canada.

The provisions of the Bell-Northern supply contract obligate Northern Telecom to supply Bell Canada with such materials as it may reasonably require for its business although Bell Canada is not obligated to purchase any such materials from Northern Telecom. Prices are to be as low as those paid to Northern Telecom by other customers for like materials under comparable conditions. To ensure compliance with this provision of the contract, prices are continuously monitored and audited annually by Touche Ross. As a policy matter, Bell has chosen to give NTL the opportunity to provide new telecommunications systems and equipment before requests are forwarded to other suppliers. In fact, the vast majority of the equipment in the network is designed and built within the Bell Group... (RTPC, T-1481, p.60).



The following excerpt from Mr. Cyr's evidence is an expansion of Bell's purchasing policy.

As we move to Bell's network, we become more involved with high technology telecommunications equipment which is complex, costly, and has to provide reliable service for many years. We are talking about high-capacity radio, switching, and transmission systems. It is in this context that outside purchase is rarely considered and then only if there are valid reasons, such as a gap in the Northern product line. In any analysis of our requirements to meet a specific need, Bell will always make a point of being aware of the latest technology available in the open marketplace through its participation in seminars and conferences around the world, either directly or through BNR. The Business Development staff is aware of the latest designs in customer services and products. The regional design authorities keep up-to-date on central office and transmission equipment available in the open market. When it is advantageous to do so, Bell will buy equipment from outside suppliers, such as transmission test equipment and PBX's. Awareness of technology and availability of products from others does not alter the fact that for network elements Bell prefers to buy from Northern. In the usual case Bell or NTL will identify the need for the introduction of new technology and work within the tri-corporate structure to introduce necessary products to meet network requirements. (RTPC, T-1481, pp.61-62).

Bell has contended that this preferred supplier relationship does not prevent Bell from purchasing superior equipment from a supplier other than Northern Telecom. This policy was formulated in more detail by Mr. Cyr at p.69 of T-1481.

Bell Canada has contended throughout the course of the inquiry that the preferred supplier relationship has resulted in many benefits both to itself and consequently to its subscribers and to Northern Telecom.



It has claimed that this relationship facilitates the sharing of proprietary information which improves the planning process at both Bell Canada and Northern Telecom, enabling Northern Telecom to conduct risky, large-scale R & D, in order to retain its position at the leading edge of technology. This was described by Dr. Hall, President and Chief Executive Officer of Bell Northern Research Limited:

Risk is a factor. Risk is minimized if you have the knowledge base and can successfully manage that knowledge base to minimize risk. Without the knowledge base, the risk is enormous. (RTPC, Vol. 192, p.29126).

In an attempt to rebut Northern Telecom's claim that the preferred supplier relationship enables it to be internationally competitive, the Director has questioned equipment manufacturers, such as Mitel, which are not party to a preferred supplier relationship, and have demonstrated their success in selling to telephone companies other than Bell. Ontario considers that such evidence does not address the issue of vertical integration of a full spectrum manufacturer and a carrier. These manufacturers produce, at most, only a few product lines and these few lines are generally terminal equipment. Ontario believes that to the extent that these manufacturers are experiencing difficulties in their efforts to sell their equipment, the problem will be addressed and dealt with by the CRTC's consideration of the terminal attachment issue in November of this year.

There does not appear to be any full spectrum manufacturer which is not enjoying the benefits of a preferred supplier relationship in at least one country -- and more than one such full spectrum manufacturer enjoys such a relationship in several countries.



Chapter 5 of Mr. Davies' submission entitled, "Nature of the Telecommunications Equipment Industry Throughout the world" (RTPC, T-1566), describes the protected market enjoyed by Northern's three largest (in terms of sales) foreign competitors -- ITT, L.M. Ericsson, and Siemens. According to Table 30 at p.71, for instance, L.M. Ericsson enjoys a protected market (which it shares with other members of the local 'club'), in Sweden, Italy, Brazil, Mexico, Spain, Venezuela, Norway, Netherlands, and Argentina. Table 31 at p.74 lists ITT's shared, but protected markets as West Germany, France, Spain, United Kingdom, Italy, Belgium, Brazil, Australia, Norway, Switzerland, Netherlands, and Austria. Siemens is described at pp.76-77 as having a large, fully protected domestic market in Germany in addition to having and sharing fully protected markets in Austria, Finland, U.K., Ireland, Norway, Sweden, Switzerland, Mexico, South Africa, Spain, Italy, Belgium, Argentina, Brazil, Greece, Venezuela, France, Colombia, U.S., and Canada.

While not conclusive, the evidence that all major competitors have such a preferred supplier relationship indicates that such a relationship is not only beneficial but likely vital to the existence of world scale, full spectrum, telecommunications equipment manufacturers.

The benefits to Bell Canada of the preferred supplier relationship fall into three categories: co-ordinated planning, co-ordinated provisioning, and product support. These were described most succinctly by Mr. Inns Executive Vice-President of Bell Canada, Ontario Region as follows:





The benefits derived during the fundamental and technology planning stages manifest themselves in the form of the co-ordinated research and development program, the Company's influence over the technology design process and computerized planning tools and methodologies developed by Bell Northern Research for use by the Company's fundamental planners . (RTPC, T-1422, p.78).

The operational benefits of the Bell Canada group relationship are illustrated throughout the forecasting and implementation facets of the provisioning cycle. In addition, procurement of telecommunications products from Northern Telecom offers advantages with respect to both price and quality control... (RTPC, T-1422, p.88).

The benefits of the Bell Canada group relationship arising during the product support stages manifest themselves in the form of direct technical support to the operations people to assist with immediate or impending service jeopardy situations, and indirect technical support in the form of technical documentation and repair services . (RTPC, T-1422, p.102).

The Director attempted to demonstrate that small manufacturers do not have access to the Bell Canada market, and that one of the problems of the current relationship is that Bell is currently purchasing equipment that is not optimally suited to its needs. The evidence on this issue is inconclusive. There are those of Northern's competitors who contend that Bell has purchased Northern equipment which was less suited to Bell's needs than was their equipment. For example, Mr. Keane, of the Vidar Division of TRW, has testified that Bell Canada has discriminatory purchasing practices.

Q. Now, you know that there is a Northern Telecom product that is competitive with your D-3 presently on the market, do you not?

A. That is right.



Q. The Northern Telecom product is called the DE-3?

A. That is right.

Q. Are you familiar with that product?

A. Relatively so.

Q. Has your Company done any comparisons between your product and theirs?

A. Yes.

Q. And you would agree with me that the Northern Telecom product compares favourably with your product?

A. Yes, it does.

Q. I suppose in some areas it might have some advantages?

A. It has one significant advantage. It has Bell Canada as a customer.

(RTPC, Vol. 20, pp. 2805-2806).

On the other hand, the testimony of Mr. Hadley of Farinon Canada Ltd. lends support to the accuracy of Mr. Cyr's previously quoted formulation of Bell Canada's purchasing policy.

Q. In the area of heavy equipment that you spoke of, of Northern Telecom, have you been able to sell Bell Canada in respect of that equipment?

A. It is a little less clear situation because the Northern Electric 6 GHz microwave equipment is what I would call a heavy-load high-capacity system and our equipment is medium-rate capacity equipment.



Q. It is not head-on competition?

A. There are projects where both systems could be put in and there have been situations where we have bid against Northern Electric on specific projects and depending upon the telephone company's feeling as to which system was more optimally suited for the application, the job has been awarded to Northern Electric or to ourselves. (RTPC, Vol.52, pp.8179-8180).

The evidence supporting the Director's allegation on this issue is, at best, inconclusive particularly in view of the trend indicated in Tables 1-4 of T-1482 which indicates that the proportion of non-Northern equipment purchases increased from 14.4% in 1975 to 19.4% in 1978. While again, not conclusive, Ontario finds this to be a significant indication that Bell is, in fact, increasing its purchases of non-Northern equipment, thereby encouraging the development of these small manufacturers.

At first glance, imposing a procurement policy of competitive bidding may appear to be a means of maintaining some of the benefits associated with a vertically integrated relationship, yet eliminate some of the alleged problems associated with the structure, without resorting to the blunt measure of divestiture.

It is respectfully submitted that this solution to a difficult public policy question is too simplistic and should not be imposed. It is Ontario's submission that it has not been shown that competitive bidding is a preferable, or even a viable, public policy option compared to the current procurement practices of Bell Canada.



Furthermore, it is submitted that the imposition of competitive bidding may be costly to Bell Canada, and consequently to its subscribers, costly to the regulator and damaging to Northern Telecom's ability to compete in the long run.

Ontario would agree that competitive bidding in the broadest sense can be an effective means of procurement for the small, non-vertically integrated telephone companies. Each of the Prairie telephone companies - M.T.S., Sask. Tel., A.G.T. and Edmonton Tel. - rely on competitive bidding to a limited extent. (R.T.P.C., Vol. 23, p.3246; Vol. 24, p.3544; Vol. 6, pp. 772- 810; Exhibit T-1226). M.T.T., N.B. Tel. and Nfld. Tel. also rely on competitive bidding. (R.T.P.C., Vol.14, pp.1956-1960; Vol. 17, 2382-2385; Vol. 60, pp. 9131-9132).

However, it is important to note that "competitive bidding" is a generic term describing a wide variety of purchasing practices. For example, the consultants hired by the Director (Consultec) to survey the procurement practices by the Prairie Telephone companies defined the scope of competitive bidding very broadly:

- Q. Let me be clear, my understanding of your definition of competitive bidding to Mr. Kaiser is roughly the same as that at page 642 of the CRTC transcript where Mr. Henderson asked you the same question?
- A. Uh-huh.
- Q. And it would include any time you go out to more than one person, however you do it, regardless of whether it is open tender or tender or anything else. As long as you ask more than one?
- A. Well, in some kind of formalized manner you ask more than one...

(RTPC, Vol. 161, p.24130)





Effectively this could cover any procurement policy, particularly when "this formalized process may mean nothing more than a letter". (RTPC, Vol. 161, p.24131). The purchasing policies of the telephone companies are indeed highly variable and the choice of procedure itself is highly subjective depending on the particular company and the type of equipment being purchased.

Competitive bidding would be very difficult to enforce for all products other than standardized products. Complex equipment is rarely purchased solely on the basis of low price; other factors are taken into consideration (e.g. quality, maintenance, compatibility, delivery etc.) Such equipment is not directly comparable. The value to the company of the heterogeneous equipment offered in the tenders may bear little relation to the price. Furthermore, the price quoted in bids to the Company bears only a partial relationship to the overall cost of the item. This is particularly true where durable equipment is purchased on the basis of its life-cycle cost. It would be very difficult, if not virtually impossible, for any outside body to second-guess the largely judgemental estimates made by engineers on both the value and the life-cycle or overall cost of equipment to the telephone company. It would mean that the regulator would assume to a significant degree some of the prerogatives of management of the telephone company.

Any attempts by a regulatory body to evaluate whether competitive bids tendered had been fairly treated would be very costly. Consider the following exchange between Dr. Roseman, member of the Commission and Mr. S Robertson of Maritime Telegraph and Telephone Company Limited.



DR. ROSEMAN: I have a number of questions, Mr. Robertson. Now, one of the areas I would like to spend a considerable time with you, even though you have already gone over the matter at some length, is the purchasing decisions. Now, one of the points you highlighted in discussing purchasing situations, was that when it comes to switching equipment you have a complex of factors that it would be virtually impossible, let us say, for outside parties to evaluate. You did not put it in those terms but that is one of the conclusions I derived from it, that there are so many judgmental factors involved that, let us say for you or one of your top executives, as experienced executives in a tel co, to go into another telephone company and say "No, that was the wrong decision", would be a very problematic kind of exercise.

THE WITNESS: It is very difficult. It can be done because you can ask for the assumptions and ask for all of the information, the current data, the future prognostications and everything else upon which it is based, and you can make a value judgment and, in fact, that is what we do internally...

To that extent, yes, you could, you can ask enough about it that you could satisfy yourself on the basis of a value judgment that it was a reasonably good decision or a good decision or apparently not one. It would be somewhat subjective, but it is possible to scrutinize it. It is not any more difficult than lots of other things that we do in the modern world in terms of making decisions. It is not easy, but it can be done. You can evaluate.

MR. ROSEMAN: Now, what other types of equipment would you put in the same category with regard to difficulty of scrutinizing a decision?

THE WITNESS: In a sense, many of the basic elements that make up a system, although I would think that a decision about a certain type of switching equipment like the CI-AEX or the SPI, would be a more complex decision. The elements in the equation would be more complex than the decision about telephone sets, terminal voice telephone devices of a standard variety, although there is complexity there too, in calculating various regions. So there would be a range, you



are quite right, and I would expect that basic switching equipment, which is really the nerve centre of telecommunications systems, and it is one of the more complex systems it enables the phenomenon of interactive address selectivity to be accomplished. It is like a computer and so, yes, I would think that that would be one of the more complex pieces of equipment upon which you would have to make such a judgment, and others would rank from that, but I could be wrong. I could be forgetting or not aware of other decisions which might be more difficult or more complex.

(RTPC, Vol. 15, pp. 2169-2071)

One practice which does appear to be consistent for all of the telephone companies is that they do not consider themselves bound to accept the lowest bid price for telecommunication equipment. Consider, for example, the following exchange between Mr. Robertson, President of Maritime Telegraph and Telephone Co. Ltd., and Counsel for the Director:

- Q. But your invitation for tendering does not in any way bind you to the acceptance of the lowest bid?
- A. That is right.
- Q. It is merely a jumping off place for negotiation?
- A. If we want to do that.

(RTPC, Vol. 14, pp.1959-1960).

Edmonton Telephones, which is required by municipal by-law to use formal, open tenders for all of its purchases over a certain size, does not consider itself bound to accept the lowest tender bid. As a consequence, there is no objective means of ensuring that the telephone companies are administering the competitive bidding procedures fairly.



The voluminous record arising out of the dispute between Bell Canada and Vidar in volumes 20, 48, 220-221 and Exhibits 109-110, 317-333, 1795, 1795A, 1862-1864, and 1867 illustrates how difficult and time-consuming any attempt to adjudicate such disputes can become.

It has also not been shown that competitive bidding, if introduced, could be enforced. If competitive bidding is introduced, it will be a costly change. And, if it is indeed unenforceable, none of the alleged benefits will result, but in fact overall costs will be increased. The Director's expert witnesses (Consultec) recommended that the competitive bidding procedure be actively regulated by the CRTC, but this is likely to impose a costly regulatory burden with no apparent benefits. (Exhibit T-1226; RTPC Transcript Vol.161 at 23999, Vol. 162 at 24261-4).

In concluding the discussion of this issue, Ontario would agree that greater access to the Bell Canada market for Canadian-based manufacturers may be beneficial. Enforcing such access either through divestiture or enforced competitive bidding, however, will likely involve greater costs than benefits.

## 2. Extension of Market Foreclosure to Other Telephone Companies

The Director has alleged that Bell Canada has attempted to use its power to influence the purchasing decisions of other telephone companies.





Bell Canada appears to have influenced TCTS in ways which have been beneficial to Northern Electric . (Green Book, p.67).

Ontario would regard such a charge, if proven, as serious as it would represent an attempt to use pure market power in an anti-competitive manner. However, the evidence presented during the case would appear to directly contradict this allegation.

Mr. Thompson, then President of TCTS, stated this categorically in the following exchange with counsel for the Director.

Q. Is there any or has there in your experience been any indication of direct Bell pressure on other members of the system to buy Northern equipment?

A. No. (RTPC, Vol. 18, p. 2661).

Similarly, evidence was given by Mr. Robertson, President of Maritime Telegraph and Telephone Company Limited.

Q. And what influence do you notice is exerted by Bell as to the choice of Northern equipment as opposed to other equipment for TCTS purposes?

A. None to my knowledge of the decisions of TCTS are undertaken on the basis of purchasing equipment from Northern Telecom. The end result might be, if we decide to use a certain thing that Northern has the best equipment, but that is not the reason why the decision is made. (RTPC, Vol.15, p.2071)



Similar denials were made by other TCTS members. Moreover, direct evidence concerning the purchasing practices of the Prairie Telephone Companies does not support the allegation of the use of such influence. Ontario must regard this allegation as unproven.

### 3. Distortion of Northern Telecom's Pricing Policy

The Director makes two allegations in this regard. The first is:

Bell Canada's vertical integration with Northern Electric has consistently been an issue of contention at Bell Canada's regulatory hearings. One issue can be summarized as a concern that Northern Electric charges Bell Canada excessive prices for equipment and, secondly, that Northern Electric's non-Bell Canada activities are accordingly subsidized by its Bell Canada activities. (Green Book, pp. 136-137).

Previously, he had argued that in order to maintain its relationship with Bell Canada, Northern Telecom was pricing its products on a "political" basis largely determined by considerations of regulatory expectation rather than those of economic efficiency.

In support of this allegation, the Director cites the following memo dated July 31, 1964 from V.O. Marquez to R.H. Keefler, both Northern Electric executives:

It seems to be worth considering, in setting our prices for General Trade, that we try constantly to be at least a little lower than the independent telephone prices in the U.S. expressed in Canadian dollars.



This is a relationship we have not sought deliberately in pricing in the past. If we used it in the future and were successful in meeting these targets across the board, we would then be in a position to say publicly that non-Bell Canadian telephone companies pay prices for communication products which are always lower than those paid by any independent American telephone company. We would also say that Bell of Canada pays prices which are always substantially lower than those paid by independent telephone companies in the U.S. (Green Book, p. 91).

While either charge would have to be considered carefully, it is difficult to know what is intended when they are presented together. It is important to note that whatever the theoretical concerns, no evidence was presented to show that Northern Telecom prices to Bell Canada were too high. The danger that Northern Telecom is being forced into inefficient behaviour as a result of its relationship with Bell Canada will be discussed in more detail further under the heading "Northern Telecom and Bell Canada's Innovativeness."

#### 4. Decreased Effectiveness of Regulation

It was also alleged by the Director in the Green Book that vertical integration increased the cost of regulation of Bell Canada, since the regulator must make certain that the effects of regulation of Bell are not being made inoperative by Bell Canada's relationship with Northern Telecom (i.e., Bell is not hiding monopoly profits in Northern Telecom). Ontario agrees that these "non-arms-length" transactions are difficult to regulate.



The mechanism used by Bell Canada to assure its regulators that the interests of the subscriber are indeed being protected is contained in its Supply Contract with Northern Telecom. This contract requires that Bell Canada be given the lowest available price for comparable equipment. The Director criticized this Price Comparison method as follows:

Given the concentrated structure of the equipment industry and the pricing conduct of Northern Electric, the price comparison tests are not an adequate test of Northern Electric's performance. That is, the exercise has shown that Bell Canada has paid the lowest available price for equipment but the exercise has not indicated whether or not this was the price which would have been charged in a competitive market or whether or not this was a proper price given existing market conditions.

(Green Book, pp.99-100)

The Director did argue that theoretically vertical integration may result in abuses, but no factual evidence was presented to support this charge.

Divestiture would reduce the complexity in regulating Bell Canada since arms-length transactions would require less regulatory involvement. However, Ontario would argue that the risks associated with divestiture renders such radical action wholly inappropriate to solve the problem of regulatory effectiveness. Ontario intends to consider this problem within the context of its submission to the CRTC concerning the terms of the Bell-Northern Supply Contract.





5. Northern Telecom's and Bell Canada's Innovativeness  
 A. Northern Telecom

The Director alleged that evidence exists that:

...indicates some serious conflicts and inefficiencies in innovative performance as well as serious distortions in allocative efficiency. The documents illustrated how historic ties with AT&T, general management conflict within the complex, and conflict in specific areas of innovative specialization and product quality all hindered the complex's innovative performance .

(Green Book, p. 185).

The concern about Northern Telecom's lack of innovativeness would not appear to be very compelling in the context of 1981 with Northern Telecom having successfully established itself as an internationally competitive manufacturer, as indicated by the following testimony of Mr. Grandy:

- Q. What is the general reputation which Northern Telecom has in Canadian circles?
- A. It has a very high reputation as the most sophisticated and innovative company in the high technology field.
- Q. Do you know of any other company which in that field has gained any recognition throughout the world as being highly innovative in this business?
- A. No.
- Q. Now, Mr. Grandy, in assessing the performance of a company, in your experience, do you assess it on a basis of one year or over a period of years?
- A. Oh, no, naturally over a period of years.  
 (RTPC, Vol. 223, pp.33504-33505).



As indicated by Mr. deGrandpre at p.33835 of the record, Northern Telecom, on May 6 of this year, was the recipient of an award presented annually to leaders in the fields of humanities and/or industrial or technological excellence by the Institute International de Promotion et de Prestige -- a Geneva-based non-government, Unesco affiliated organization. The Award to Northern represented the second time that a North American Company was the recipient, the last recipient being IBM in 1971.

This allegation of the Director has definitely not been proven.

B. Bell Canada

In an attempt to demonstrate that Bell Canada has been operating less than optimally, the Director produced as a witness, Dr. Robert Babe, Associate Professor of Communications Studies at Simon Fraser University. He performed a study which concluded first that non-integrated telephone companies experienced higher productivity gains than did the vertically integrated telephone companies for the period studied, and second, that vertical integration creates incentives for inefficiency on the part of the operating company (RTPC, Vol. 84, p.13412).

Dr. Babe's credibility was discredited at pages 13671-13679 of the transcript, where it became apparent that he is not well versed in the literature on productivity measures. His lack of knowledge in the area was manifested



in the development of a 'unique' productivity index -- unique in the sense that nothing similar to it had ever been used before, to measure a very complex concept. His lack of knowledge in such areas as equipment manufacturing, and economies of scale in the telecommunications industry, became evident during cross-examination.

Without reporting all of the many technical problems and problems of logic associated with Dr. Babe's study, the following represents examples of the inadequacies of his study:

Dr. Babe made the simplistic assumption that the source of productivity gain is primarily technology, thereby failing to neutralize for differences in the various telephone companies' opportunities to make productivity gains. Specifically:

- . The choice of the period selected can make a significant difference on the results, as demonstrated by Bell at pp. 17221-17228 of the transcript.
  
- . The study failed to account for differences in the rate of demographic changes and of opportunities to expand into new georgraphic areas.



- . The study failed to take into consideration the fact that the degree of excess capacity in the base year would affect the opportunity to make productivity gains.

It is Ontario's belief that the Director failed to prove that vertical integration inhibited Bell Canada's ability to be productive. The Director has failed then in his attempts both to prove that Northern Telecom's ability to be innovative has been hampered by vertical integration, and that Bell Canada's ability to be innovative has been hampered by vertical integration.

#### 6. Reduction in User Choice

This issue has already been the subject of the Commission's deliberations regarding the removal of the restrictions on the attachment of customer provided equipment and will, therefore, not be considered in this final argument. Ontario supports the trend towards the opening of the terminal market to firms other than Northern, and has already expressed its continuing concern to the Commission regarding the absence of reciprocal access to the market of potential foreign-based suppliers.

Ontario will fully present its views on this matter at the C.R.T.C. hearing next November, called for the purpose of considering this issue and all its implications.





PART V

CONCLUSION



Canada, its governments and its business and industrial leaders, have been undergoing a period of intense self-examination in recent years in order to determine what is required to encourage and enhance the ability of Canadian industry and business to compete effectively in the world marketplace. Many have stated that what Canada requires is a coherent industrial strategy. Northern Telecom's success in the world marketplace is pointed to as a model for what is desired for other industrial enterprises. The result of this proceeding should not and cannot be to undermine the achievements of one of the very few industries which has demonstrated its ability to compete internationally. An innovative and efficient telecommunications industry, moreover, is critical to the development of the Canadian economy since it provides the means for the creation of a wide variety of information intensive industries.

The Director has made the following allegations:

1. That Bell has foreclosed its market to competition or equivalently that Bell Canada's procurement policy favours Northern and prevents it from purchasing the most appropriate equipment available on the market.
2. That Bell has attempted to foreclose other telephone companies' markets to competition.
3. That Northern Telecom's pricing policy has been distorted.
4. That vertical integration renders the regulation of Bell Canada ineffective.



5. That Northern Telecom and Bell Canada's incentive and ability to innovate have been reduced.
6. That telephone subscribers have had a reduced choice in the equipment available to them.

In reviewing the record produced for this case, Ontario has come to the conclusion that the Director has failed to show that divestiture or an alternative such as an open tendering system is in the Canadian national interest. In particular, he has failed to seriously address the danger that the major benefactors of the abrupt opening to competition of Bell Canada's market will be large foreign-based suppliers, and that the resulting shift in market share will undermine Northern's ability to compete internationally. He has failed to demonstrate that an opening of the Bell Canada market would not negatively impact on employment; and, he has also failed to rebut successfully evidence which indicates that vertical integration is beneficial to Canada's telecommunication industry as a whole.

Ontario's position with regard to vertical integration is consistent, with the sentiments expressed by Mr. Ivan Duvar, Chairman and President of Island Telephone Company.

In summary, the combination of vertically-integrated suppliers and competition available in Canada today would appear to us to be a good balance between competitive pricing, economies of scale and system integration and we believe it should be continued in the best interest of the telephone customer until such time as there is a proven better way of operating. (RTPC, Vol.62, p.9519)

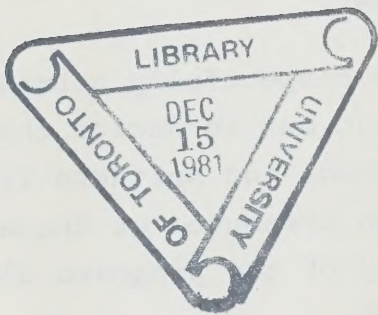
(emphasis added)



Ontario also submits that since the initiation of these hearings in 1977, a lot of factors have served to improve the competitive environment for telecommunication equipment manufacturers. One significant example was the CRTC decision liberalizing terminal attachment.

Section 19 (2) of the Combines Investigation Act requires that the Commission's Report "shall review the evidence and material, appraise the effect on the public interest of arrangements and practices disclosed in the evidence and contain recommendations as to the application of remedies provided in this Act or other remedies".

Ontario respectfully submits that the Commission has no choice but to decide that the relationship between Bell Canada and Northern Telecom be maintained. The evidence presented at these hearings has not shown that any of the proposed alternatives are in the public interest.





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